



## COUNCILMEMBER CARL DEMaIO

FIFTH DISTRICT  
CITY OF SAN DIEGO

### MEMORANDUM

DATE: May 20, 2010

TO: Andrea Tevlin, Independent Budget Analyst

FROM: Councilmember Carl DeMaio

RE: FY 2011 Budget Recommendations and Priorities

---

At the request of Councilmember Tony Young, the Chair of the Budget and Finance Committee, I am submitting my budget recommendations priorities memo to the Independent Budget Analyst for the FY 2011 budget.

In December of 2009, I provided my budget priorities for the 18-month budget being considered at the time. At that time, the FY 2011 budget balanced a projected \$179 million deficit "through one-time solutions of \$96.5 million and recurring resources of \$82.6 million."<sup>1</sup>

I also noted my desire to replace one-time deficit fixes with structural solutions, as one-time fixes do not address the core problem that the City continues to live beyond its financial means. I reiterate my desire to halt our continued reliance on one-time fixes that do not solve the structural spending issues plaguing our budget.

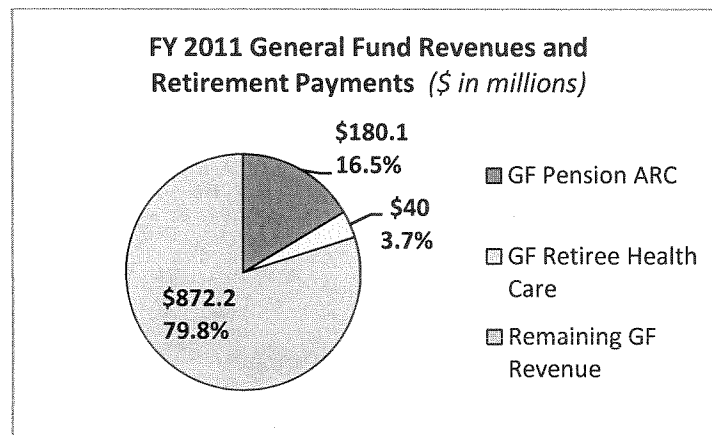
Excluding the approximate \$4.5 million budget gap needing to be solved with the May Revision, the proposed FY 2011 budget still features corrective actions of \$28.2 million, \$14.1 million of which are considered to be one-time actions by the IBA.

Furthermore, the updated Five Year Outlook projects significant budget deficits (\$48.1 million - \$72.5 million) in each year covered, before accounting for the underfunding of retiree health care and deferred maintenance/capital liabilities.

My concern is underscored by the continuation of an unsustainable relationship between the City's annual retirement obligations and the General Fund. Using the data provided in the updated Five Year Outlook, the following pie chart provides a proportional look at FY 2011 General Fund revenue compared to funding of pension and retiree health care obligations.

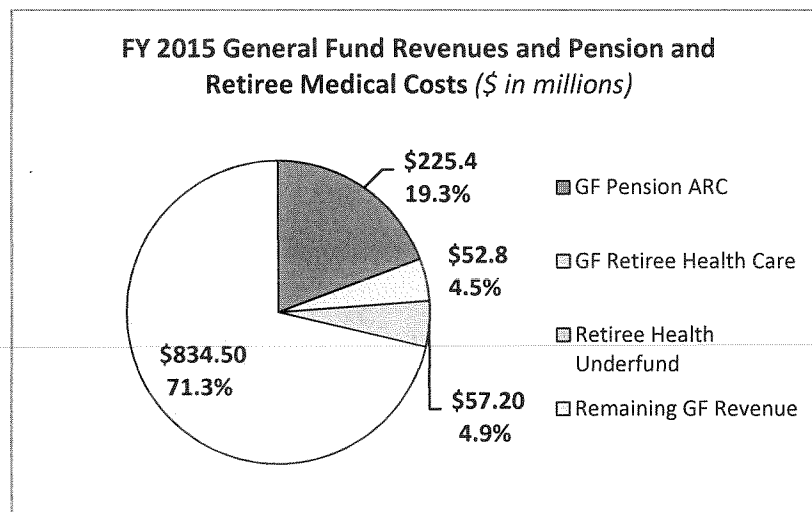
---

<sup>1</sup> See IBA Report 09-90.



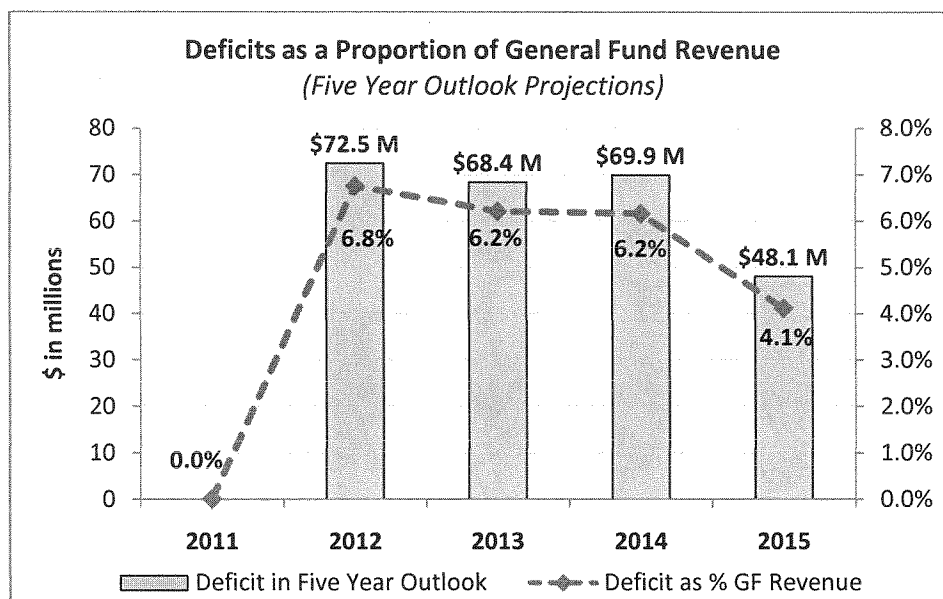
As the chart above shows, for the FY 2011 Budget, after funding the General Fund pension obligation and *paying only 48% of the actuarially required retiree medical obligation*, less than 80% of the City's General Fund revenue remains.

The chart below depicts how this picture changes if the retiree medical obligation is fully funded. Using the FY 2015 projections from the Five Year Outlook, but assuming that retiree medical costs are fully funded yields the following scenario for FY 2015 (the last year in the most recent Five Year forecast)<sup>2</sup>:

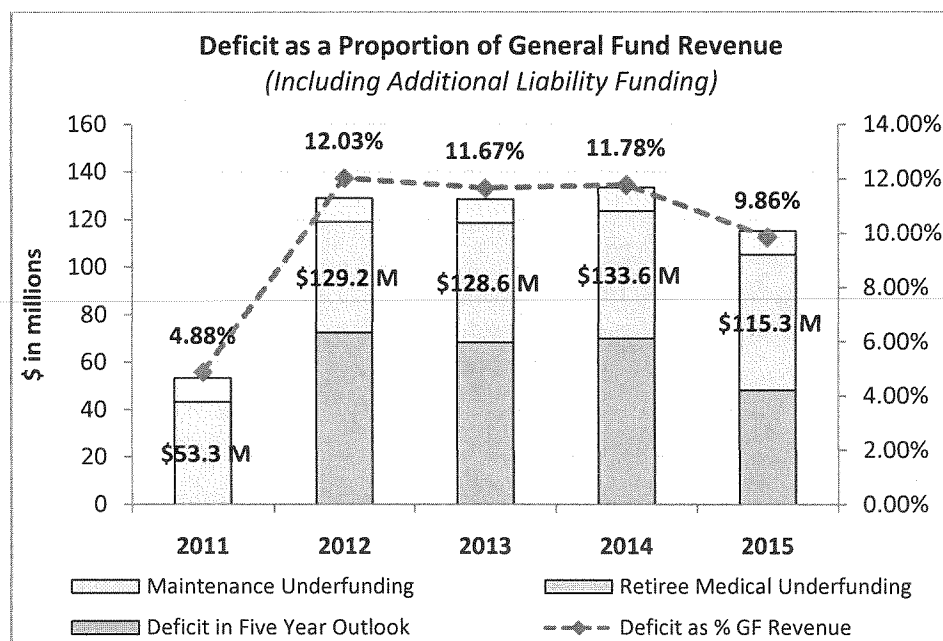


It may also be useful to examine the City's forecasted deficits in a proportional comparison to the City's General Fund. The chart below shows the projected General Fund deficits according to the updated Five Year Outlook.

<sup>2</sup> Assumes that projected General Fund retiree medical payment equates to 48% of full General Fund cost in FY 2015.



The data in the above chart shows that even after \$207.2 million in cumulative corrective actions for the FY 2011 budget, the City does not face a deficit of less than 4% of its entire General Fund for the remainder of the Outlook – *before accounting for the underfunding of significant liabilities*. As shown below, accounting for these two liabilities significantly worsens the deficit outlook significantly.<sup>3</sup>



Incorporating the retiree medical and infrastructure liabilities into the forecast shows that the City has projected deficits near or above 10% of its annual General Fund revenue in each year of the Five Year forecast.

<sup>3</sup> Maintenance underfunding for ongoing maintenance needs and additional capital needs amortization assumed at \$10 million annually. This number will hopefully be clarified by an anticipated June report.

My priorities for the FY 2011 budget are as follows:

### **1. Book the City's True Liabilities in Deficit Calculations**

Continuing to omit retiree health care and infrastructure liabilities from annual deficit calculations for annual budgeting and financial forecasting purposes **does not mean that these liabilities do not exist**. In 2004, the Pension Reform Committee Final Report noted:

"The [pension] UAAL has been treated as off balance sheet debt when in fact it is a full obligation of the City."

The current treatment of these two obligations repeats this same error. Unless reforms are solidified with respect to retiree health care, the same holds true with that liability.

As it pertains to annual infrastructure maintenance funding, I disagree with the notion that the City does not have an obligation to taxpayers to adequately maintain public assets. This means that regular maintenance costs are in fact an annual obligation of the City, as well as the amortized reduction of the deferred maintenance/capital backlog. Failing to do so pushes current obligations on to future taxpayers and perpetuates a generational inequity – a practice I cannot support.

Adding these two significant liabilities to the City's deficit total will have the effect of increasing budget transparency and more clearly depicting the reality of the City's financial condition.

### **2. Reform the City's Pension, Retiree Health and Deferred Infrastructure Liabilities**

#### **Pension Reform**

Since my last submission on pension reform in December, the City Attorney has sought legal remedy to compel SDCERS to comply with City Charter Section 143.1. While we await the outcome of these efforts, the pension reform goals I presented in December still hold today:

- a) Reducing the pension debt through benefits reform,
- b) Reducing the pension debt through reforms that achieve actuarial savings (managed competition, salary freezes, reductions-in-force, etc.)
- c) Achieving savings in other parts of employee compensation to pay down accrued pension liabilities, or
- d) A combination of all of the above.

Furthermore, the City can pursue reform of the following discretionary items:

- Negotiating a SPSP waiver option for the Local 127 and any unclassified employees still receiving the benefit.
- Eliminating all Employee Offsets, or “pickup” that remains. While the steps taken to eliminate the offset for some employees are commendable, the proposed FY 2011 budget includes \$7.9 million in offsets (\$4.8 million General Fund).
- Negotiation of a new pension plan for remaining bargaining units. A reformed pension benefit package for new hires has not yet been implemented for all bargaining units. A more affordable benefit must be negotiated as soon as possible with all remaining bargaining units that do not yet have a reformed pension plan for new hires.
- Increase employee contribution rates to reflect a fair share of market losses.

The City must also closely monitor the progress of the City Attorney’s actions, as well as prepare for additional reform opportunities that may arise in the event of updated determinations by the Internal Revenue Service (IRS) with regard to individual employee opt-out capability. While these events materialize, however, the City can and should adamantly pursue the reforms provided above in the coming year.

### **Retiree Health Care**

The previous analysis of the difficulty associated with balancing the City’s budget when accounting for the full cost of current retiree medical benefits displays the crucial nature of reforming of this liability. Following the completion of the ongoing “Joint Study,” the City must aggressively negotiate to ensure that meaningful reform is achieved in this area.

## **3. Other Structural Reforms**

### **Managed Competition:**

As of May 20, 2010, it has been 3 years, 6 months and 13 days since voters approved the Managed Competition reform tool in the City of San Diego. Immediate action to implement this critical reform tool is necessary, and has been called for by taxpayers for more than 3.5 years.

The Mayor should be given the authority to proceed with competitive sourcing for a number of functions – including trash collection, landfill management, auto maintenance, landscaping, printing/publishing and information technology. Consistent with this authority, the City Council should support the Mayor in the necessary “Meet and Confer” process with our labor unions.

### **Performance Audits**

I am pleased to have proposed six performance audits with my Council colleagues last week. Continuing to support the efforts of our City Auditor in identifying available cost savings and prudently following up on the recommendations of audits must be prioritized.

### **Enhanced Marketing Partnerships**

The City should expand its marketing partnerships to generate additional revenues. This concept has also been endorsed by the Teamsters 911 bargaining unit. I plan to submit a detailed proposal on this idea in the coming weeks.

### **Elimination of Terminal Leave**

Earlier this year, the City Council took final action to eliminate Terminal Leave for three groups of employees, but has not yet eliminated it for a number of bargaining units. This costly benefit represents another opportunity for the City to reduce its costs associated with discretionary benefits.

## **4. Jobs Friendly Environment**

### **Reject Tax and Fee Increases**

The City must avoid increasing taxes and/or fees, as these revenue increases place additional hardship on San Diego's working families and businesses.

### **Improve Small Business Efforts**

The technical assistance provided by organizations such as Business Improvement Districts (BIDs) can be improved upon by examining the ways in which the City interacts with them. Rather than engaging in overly burdensome reimbursement processes, the City should explore a forward-looking budgeting process for the BIDs to provide these organizations with increased cash flow certainty and reduced administrative burdens. At the same time, the City can maintain adequate administrative oversight by exploring a change to the current governance model of the BIDs.

The City should also seek to reduce the burdens associated with regulatory compliance that it places on small businesses. Increased automation of the permitting process is an essential place to start this reform effort.

As the daunting deficit projections make clear, quickly pursuing needed reforms is critical to the City's financial health. I look forward to working toward implementing these reforms in the coming year.